



MICHIGAN HEALTH & HOSPITAL ASSOCIATION

Advocating for hospitals and the patients they serve.

House Health Policy, February 23, 2009

Testimony before the House Health Policy Committee

Impact of Economic Recession and Credit Crisis on Michigan Hospitals and Patients

David Seaman, executive vice president, Michigan Health & Hospital Association

I appreciate the opportunity to meet with you today to discuss the fiscal crisis facing Michigan's 144 community hospitals.

It is not an overstatement to describe the current environment as the "perfect storm" for health care.

- State and National recession (many suggesting the worst since the Depression)
- Credit market collapse (unprecedented)
- Burgeoning unemployment (Michigan #1)
- Record Medicaid caseloads
- Rapidly deteriorating hospital margins

The crisis faced today is unlike any witnessed in the recent history of our state and requires actions unlike any that we have undertaken in the past.

In Jeopardy:

The publication before you, "Michigan's Health Care Safety Net: In Jeopardy" paints a very bleak picture describing five adverse impacts growing out of the economic collapse.

1. Skyrocketing Uncompensated Care

2007: \$2 Billion in unreimbursed care

a. Components

- i. \$209 Million in charity care (no ability to pay)
- ii. \$605 Million in bad debt (unable/unwilling to pay)
- iii. \$1.2 Billion in unreimbursed costs of government programs

b. The worst is yet to come

- i. 2008 Survey shows a 40% increase in charity care (could represent a nearly \$100 million add-on loss)

SPENCER JOHNSON, PRESIDENT

CORPORATE HEADQUARTERS ♦ 6215 West St. Joseph Highway ♦ Lansing, Michigan 48917 ♦ (517) 323-3443 ♦ Fax (517) 323-0946
CAPITOL ADVOCACY CENTER ♦ 110 West Michigan Avenue, Suite 1200 ♦ Lansing, Michigan 48933 ♦ (517) 323-3443 ♦ Fax (517) 703-8620
www.mha.org

2. Negative Margins
 - a. Margin is the measure of cost of care versus revenues.
 - b. Negative 2.9% Total Margin = a recipe for disaster.
 - c. This means that Michigan hospitals, on average, are losing money, and no one here needs to be reminded of what happens when expenses exceed income.
3. Construction Halted
 - a. Numerous facilities have halted current or planned construction.
 - b. Important, but costly investments in Information Technologies and Electronic Medical Record development are being suspended.
 - c. These required withdrawals jeopardize hospital's abilities to address changing standards of care and invest in projects to improve quality and patient safety.
4. Workforce Layoffs
 - a. Health care = the state's largest private sector employer
 - i. 515,700 direct jobs and 278,500 related jobs
 - ii. Nearly \$37 billion in wages and benefits
 - iii. \$12 billion in taxes
 - b. This workforce is threatened:
 - i. Over 1300 jobs lost in 2008 through layoffs or attrition
 - ii. Teaching programs to grow the workforce of the future are threatened
 - iii. Recent drain of young, talented students to other states continues
 - iv. And more bad news will surely follow
5. Record Medicaid Caseloads
 - a. Hospitals are the state's health care safety net, and with apologies to BCBSM, the fact is the *real* "insurer of last resort" is the hospital Emergency Room
 - b. 46% increase in Medicaid recipients since 1999 – there are now 1.6 million Medicaid recipients in Michigan (nearly 1 of every 6 Michigan residents)
 - i. nearly half of the recipients are infants and children under 18
 - c. At the same time, rates have not been increased in nearly a decade, and hospitals accepted a tax to help the State draw down federal dollars to assure ongoing coverage for our most vulnerable citizens.

Closing Observations:

Before closing, I would leave you with the following observations:

- The crisis facing Michigan hospitals is very real and has far-reaching consequences.
- Michigan's nonprofit community hospitals provide a unique set of benefits to the state providing jobs, creating opportunities for economic development, and most importantly serving as the health care safety net, providing access to all, 24 hours a day, 7 days a week, 365 days a year.

- The call for hospital services is counter cyclical, meaning the need for care in hospitals increases when the economy softens, when people lose their jobs and health benefits, and when individuals delay seeking care until they are acutely ill. Never has the expectation or need for hospital availability been greater.
- Historic underfunding by governmental payers has severely stressed the providers of health care, causing increasing numbers of physicians to withdraw from the Medicaid program and increasing the pressure on the hospital community to fill the void.
- Government underfunding has also given rise to “cost shifting” to employers, whose response has been to necessarily increase co-pays and deductibles and increasingly has led to wholesale elimination of employer sponsored health coverage.
- Monies from the federal stimulus package represent a critical tool to help stabilize a teetering health care system, but plans are afoot to divert these monies which are, by design, intended for health care.
- The proposed budget alleges to “hold hospitals harmless,” but the record shows that hospitals have and continue to be harmed.
- Now, more than ever, we must direct funding to the most critical governmental services, and funding to preserve the health of our state must be at the top of that list.

I thank you for the opportunity to appear before you this morning and I welcome your questions.

A MICHIGAN HEALTH & HOSPITAL ASSOCIATION SPECIAL REPORT

MICHIGAN'S HEALTH CARE SAFETY NET:

In Jeopardy



*The Impact of the Economic Recession and Credit Crisis
on Michigan Hospitals and Patients*



February 2009

Introduction

Michigan's 144 community hospitals are on the brink of a fiscal crisis brought on by the state and national recession, the credit market collapse, and a growing number of patients who are unable to pay for their health care. These recent developments are placing an additional burden on Michigan hospitals, already strained by years of underfunding from the state Medicaid, Medicare and other government programs.

As Michigan hospitals struggle to remain viable, the impact is painful, and in nearly all instances, human. Most alarming, the economic circumstances are worsening, affecting more patients and communities across the state.



The mission of Michigan hospitals is to care for all who pass through their doors, regardless of their ability to pay.

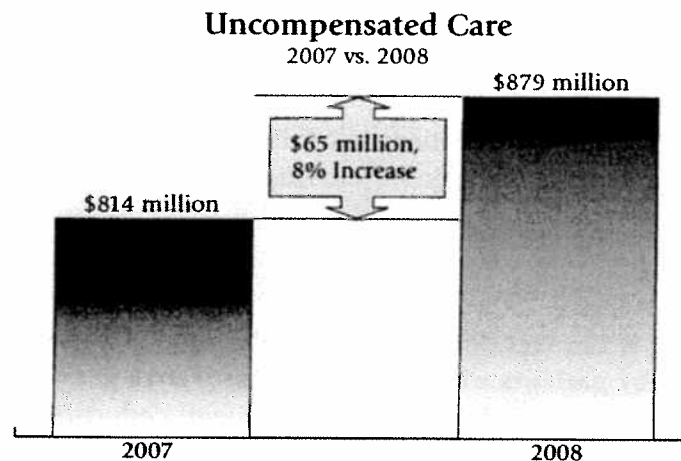
That mission is now seriously threatened, as are health care services for the patients who seek treatment in Michigan hospitals millions of times each year. Also threatened are thousands of jobs in the health care sector, which now ranks as Michigan's largest private employer.

In addition to fulfilling their mission as the state's health care safety net, Michigan hospitals collectively advance public policies that seek to maximize **Access** to health care services, keep health care **Affordable**, improve the **Quality** of

health care services, and improve the **Health Status** of Michigan citizens. As the new Michigan Legislature and U.S. Congress convene, it is important that our elected leaders understand the human, economic and public policy consequences of a financially weakened hospital sector. For years, Michigan hospitals have urged Lansing and Washington to fund their fair share of health care through adequate Medicaid and Medicare appropriations. Government underfunding of health care has now collided with the worst recession since the early 1980s and possibly since the Great Depression, bringing still further pressure to the state's hospital safety net that has not been this fragile in generations.

A Michigan that fails to deliver access to affordable, high-quality health care is a Michigan that cannot recover, compete or prosper economically.

Impact #1: Skyrocketing Uncompensated Care



Source: 2008 MHA Community Benefits Survey and the MHA Monthly Financial Survey

In 2008, Michigan hospitals absorbed record amounts of uncompensated care, surpassing the previous year's unprecedented levels. Uncompensated — or unreimbursed — care includes bad debt¹ and charity care² provided by hospitals for which they are not paid.

In 2007 (the most recent full-year data available), Michigan hospitals provided more than \$2 billion in unreimbursed care. That figure includes more than \$605 million in bad debt, \$209 million in charity care, and \$1.2 billion in unreimbursed cost of health care services provided to patients covered by Medicaid, Medicare and other government-sponsored programs.

Dozens of Michigan hospitals confirmed that uncompensated care increased again in 2008. A survey³ of Michigan hospitals in December 2008 found an 8 percent increase in uncompensated care in the third quarter of 2008 compared to the same period in 2007. The American Hospital Association (AHA) also reported the same increase at hospitals nationwide during this same period.

The survey also found charity care at Michigan hospitals had increased by 40 percent, a consequence of more Michigan citizens lacking the financial resources to pay for the hospital care they received.

¹ Actual or expected uncollectible funds resulting from the extension of credit.

² Health services that were never expected to result in cash inflows. Charity care results from a provider's policy to provide health care services on a free or discounted basis to individuals who meet certain financial-need criteria.

³ MHA Monthly Financial Survey as of Dec. 16, 2008, for 54 hospitals.

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A significant amount of uncompensated care can be traced directly to the recession and to a growing number of patients with no health insurance who are seeking treatment in Michigan hospital emergency rooms (ERs), which are the community's last resort for health care. In 2007 (the most recent full-year data available), Michigan hospitals recorded 4.5 million ER visits, a 3 percent increase — or 142,000 more patients — than the year before. A survey of Michigan hospitals in late 2008 found an increase of 2 percent in ER visits from the same period in 2007, so the upward trend continues and the financial pressures mount.

Many of the newly uninsured patients are former workers in Michigan's slumping manufacturing industry whose health care insurance disappeared with their jobs. In the past eight years, Michigan has lost a devastating 535,000 jobs. According to the U.S. Census Bureau, between 1999 and 2007, the number of Michigan citizens covered by private insurance dropped by a staggering 727,000 people.

Also troubling is the fact that increasing amounts of uncompensated care are being generated by patients who have health insurance provided through their employers. In growing numbers, hospital patients with deductibles and co-pay plans are receiving treatment, but are unable or unwilling to pay their deductibles or co-pays, driving uncompensated care even higher.

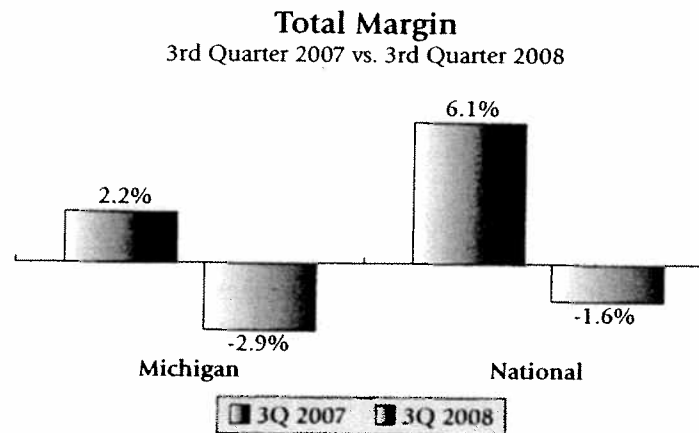
According to the 2008 Employer Health Benefit Survey released by the Kaiser Family Foundation and the Health Research & Educational Trust, many more workers are facing higher deductibles in their employer-provided health plans. The survey found 18 percent of all covered workers now have plan deductibles of at least \$1,000, up from 12 percent in 2007. In small businesses, with three to 199 workers, more than one in three (35 percent) covered workers are now called upon to pay at least \$1,000 in out-of-pocket expenses before their plan will begin to cover a share of nonpreventive health care bills, rising from 21 percent in 2007. Employers are also shifting more premium costs to workers. U.S. workers, on average, are now paying \$3,354 annually out of their paychecks to help pay the premiums, the Kaiser survey found.

Looking to the future, employers will continue to push more health care costs onto workers. A September 2008 survey by Mercer, a human resources consulting firm, found 59 percent of employers will take steps to reduce their health care costs in 2009, raising deductibles, co-payments, co-insurance, or out-of-pocket spending limits and transferring these costs to their employees. These changes will likely result in fewer families being able to pay their increased share of the cost and hospitals providing more uncompensated care.

In large part because of increasing uncompensated care, more Michigan hospitals are unable to cover the cost of care. Low — even negative — hospital margins are forcing hospitals to cut costs by eliminating services; delaying needed infrastructure, technology and equipment improvements; and paying higher interest rates to borrow.

Impact #2:

Negative Margins, Hospitals Unable to Cover Costs



Source: Databank, known in Michigan as Monthly Financial Survey, 54 Michigan and 557 national hospitals reporting for both periods.

Simply stated, a hospital's margin is the amount by which revenues exceed costs. Michigan's community hospitals use their margin to support their community mission and invest in infrastructure, new technology and equipment to improve patient care, maximize operational efficiencies, meet new health and safety requirements, and more.

Financial experts say a reasonable margin is necessary to sustain a hospital's ability to carry out its community mission and to invest in these necessities. Hospitals with sufficient margins tend to have good credit ratings, and therefore, can borrow money at affordable rates for necessary infrastructure improvements. By contrast, a hospital with insufficient margins is in financial jeopardy, and in turn, its community safety net capacity is in jeopardy.

Information from an AHA survey for the third quarter of 2008 showed that hospital total margins nationwide had slumped to *negative* 1.6 percent from positive 6.1 percent during the comparable period in 2007. For Michigan hospitals, the third quarter caused even more concern, with the statewide total margin being reported⁴ as *negative* 2.9 percent, down from a positive 2.2 percent during the comparable period in 2007, signaling further trouble for Michigan hospitals.

⁴MHA Monthly Financial Survey as of Dec. 16, 2008, for 54 hospitals.

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In late 2008, two of the nation's major credit rating agencies downgraded the bond ratings of nonprofit hospitals. Fitch Ratings revised its outlook on the nation's nonprofit hospital sector from stable to negative and attributed the downgrade to investment losses, increasing uncompensated care and higher costs for borrowing. The rating service also said, "Further state and federal budgetary pressures stemming from the economic downturn are anticipated to constrain governmental reimbursement programs, while the business sector is expected to continue to shift health care costs to its employees."

In addition to Fitch, Moody's Investor Service issued a report showing an alarming increase in bond rating downgrades for nonprofit hospitals. Moody's attributed the spike in poor ratings to increased uncompensated care due to higher unemployment, a decrease in the number of patients with health insurance, and declining revenue as patients defer elective procedures.

In spite of Michigan hospitals becoming more efficient, they are experiencing lower margins than the nation, as many payers do not reward hospital efficiency. The cost of care at Michigan hospitals is lower than national averages and lower than hospitals in surrounding states. A 2008 study⁵ by noted health care economist Harold Cohen, PhD, found Michigan hospital costs were 6 percent lower than the national average in 2006 (the most recent full-year data available at the time of the study). Michigan hospital costs also ranked second lowest among the six Great Lakes states. Cohen found Michigan citizens paid \$1.3 billion less in hospital costs in 2006 than if the state's hospital costs were at national averages. As a result, Michigan employers saved more than \$650 million.

The increase in uncompensated care, government underfunding of health care and the collapse of the world credit markets are pushing more hospitals' margins into dangerous negative territory. As a result, many hospitals are delaying needed capital and technology projects. In some instances, projects already under way are being halted because the costs of borrowing have skyrocketed or funds simply are no longer available to borrow.

A November 2008 survey of U.S. hospitals by the AHA found:

- Hospitals paid 15 percent more (\$252 million) in interest on borrowed funds in the third quarter of 2008 compared to the same period in 2007.
- 56 percent of hospitals are reconsidering or postponing facility and equipment improvement projects.
- 45 percent are delaying purchase of clinical technology or equipment.

Hospitals must maintain and improve their physical plants, infrastructures and technologies for the same reasons public universities or automakers maintain and improve their facilities and homeowners replace their roofs or carpeting.

⁵Available at www.LowerHospitalCosts.org.

Impact #3: Hospital Construction Halted

Michigan hospitals are used by thousands of people, 24 hours a day, seven days a week, 365 days a year. Most Michigan hospitals were constructed during the 1940s and 1950s. Since that time, Michigan's population has grown and aged, and as a result, Michigan hospitals are treating a higher volume of patients with more complex ailments than ever before. Because of the constant use, hospital buildings and grounds eventually require significant improvements or must be entirely replaced.

Hospital buildings also must be updated to conform to today's standards of patient care, to accommodate the changing capability of medicine and to address heightened patient expectations. New facility, patient safety and privacy standards; emergency preparedness standards; and demands for new lifesaving technology often require a hospital to make significant capital improvements. Retrofitting this new technology in outdated buildings is often more costly and less efficient than constructing new buildings or facilities.



With Michigan facing more painful state budget decisions in 2009 and 2010, the recession expected to last at least through early 2010 and uncompensated care increasing, hospital margins will continue to hover from low to negative. Elected leaders must avoid actions that reduce payments to the point of Michigan hospital insolvencies, resulting in their inability to meet patient and community needs.

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Impact #4: Hospital Workforce Layoffs

Michigan's health care sector has been a bright spot in the state's nearly decade-long recession that began in 2000.

Even as Michigan's unemployment rate has led the nation nearly every month this decade, the health care sector has consistently added jobs. In fact, health care has grown to become Michigan's largest private-sector employer, providing 515,700 direct jobs and

278,500 related jobs that inject nearly \$36.7 billion a year in wages, salaries and benefits into the economy, according to a study released in June 2008⁶ by the Partnership for Michigan's Health. Michigan health care workers and their employers also pay about \$12 billion annually in state and federal taxes, the study shows.

But in 2008, even health care employment showed signs of a slowdown, and for the first time in decades, Michigan hospitals were forced to lay off workers in a widespread fashion. At least 1,320 employees were laid off by 15 different Michigan hospitals. Beaumont Hospital in Royal Oak shed 500 jobs. St. John Health in Detroit eliminated 400 positions. Genesys Regional Medical

Center in Grand Blanc and Ingham Regional Medical Center in Lansing each cut 100 workers, and the list of hospitals furloughing 10, 15 or 20 workers at a time began to accelerate. This does not include reductions to staff hours as demand for elective procedures waned.

In addition to driving the state's unemployment rate higher, some hospital layoffs also reduce access to health care services in their communities. As part of their financial turnaround plans, Beaumont Hospitals delayed a proton beam cancer therapy center and Sturgis Hospital cut 20 jobs and closed three clinics.

Michigan hospitals are not alone. In a November survey of their members across the country, the AHA reported that 53 percent of hospitals plan to reduce staff to help balance the budget. In 2009 and 2010, Michigan hospitals will face the potential of more layoffs despite the growing number of uninsured Michigan citizens, the increase in hospital ER visits and the heightened importance of the community hospital as the health care safety net for all Michigan residents.

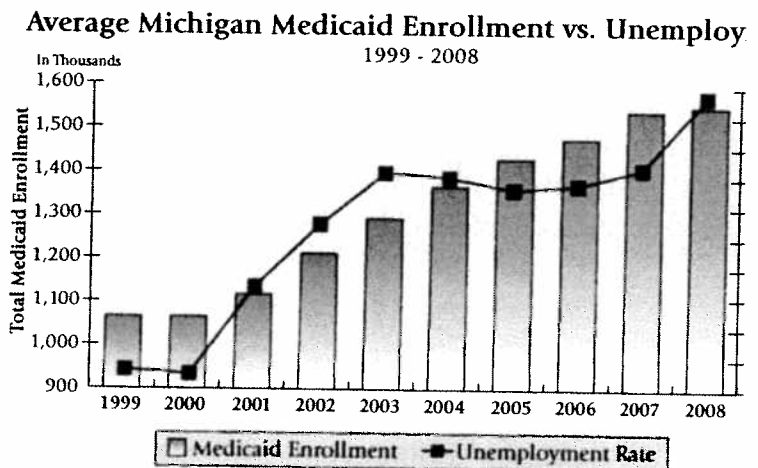
⁶Available at www.EconomicImpact.org.

Impact #5:

Record Medicaid Caseloads, Medicaid Funding Down

More than a half-million Michigan residents have lost jobs this decade. Many lost their health insurance at the same time and now depend on the state Medicaid program for their health care. In spite of record Medicaid caseload increases, Medicaid funding has been slashed.

Michigan's Medicaid caseload increased every year from 2000 — when the state officially went into recession — to 2008. In fact, the caseload increased every month in 2008 to an alarming 1.6 million people in September. Based on available data, the September 2008 Medicaid caseload was the highest in Michigan's history. The number of Michigan citizens now relying on Medicaid for their health care is a staggering 47 percent higher than in 1999. **More than one of every seven Michigan citizens now relies on Medicaid for their health care, with nearly half of them being infants and children younger than age 18.**



The national recession is expected to drive Medicaid enrollments even higher in 2009 and beyond. Enrollment will increase nationwide by 3.5 percent in 2009, according to the Kaiser Commission on Medicaid and the Uninsured. Using the 3.5 percent estimate, Michigan's Medicaid enrollment will increase by approximately 50,000 in 2009. The Centers for Medicare & Medicaid Services, in its first annual report on the financial outlook for Medicaid, is projecting an average annual enrollment increase of 1.2 percent over the next 10 years.

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But while Michigan hospitals are being asked to care for a rapidly expanding number of Medicaid patients, funding for Medicaid hospital patient care has been slashed by more than \$850 million since fiscal year 1996.

According to a December 2008 study by Milliman Inc., an independent consulting firm, government underfunding leads to significantly higher health insurance costs for employers and consumers. The study found that annual health care spending for an average family of four is \$1,788 greater than it would be if Medicaid and Medicare paid hospitals and physicians similar rates to those of private employer health insurance. This "hidden tax" on employers and consumers totals nearly \$89 billion annually, the study found.

If any positive news can be found, it is that in fiscal year 2009, Michigan will receive \$1.52 from the federal government for every \$1 invested in the Medicaid program. This federal matching rate reflects Michigan's worsening economy. However, if the state government cuts \$100 million from the state Medicaid general fund contribution, Michigan providers and their patients will be denied \$252 million in essential federal matching funds.

Conclusion

Michigan hospitals continue to provide two critically needed services in support of state residents. First and foremost, Michigan hospitals continue to provide access to care 24 hours a day, seven days a week for all, regardless of their ability to pay. Additionally, health care continues to represent a growth sector and hospitals provide opportunities for future employment growth, while the state is suffering the nation's highest unemployment rates.

To continue to ensure the viability of Michigan hospitals, it is incumbent that state and federal elected officials take four specific steps:

- pass a second federal stimulus package to bring critically needed federal funding to Michigan, a state devastated by the loss of hundreds of thousands of manufacturing jobs and skyrocketing Medicaid caseloads
- ensure that federal funds obtained through the federal Medicaid matching formula be directed to health programs as intended
- maintain the current State General Fund Medicaid funding to ensure continued access and treatment levels for Medicaid patients
- approve rate increases or specialized funding initiatives for Michigan providers to reverse the decade-long trend of provider reimbursement freezes and cuts

Recession Hammers Michigan Hospitals

Here are some of the economic indicators pushing Michigan hospitals to the brink of financial crisis:

- Between December 2007 and November 2008, Michigan lost 113,000 jobs, the steepest decline in 18 years. (Source: Michigan Department of Labor and Economic Growth, *Detroit Free Press*)
- **Michigan's Medicaid caseload has increased every year this decade. In 2008, the caseload increased every month, reaching a record high of 1.6 million recipients in September.** (Source: Michigan Department of Human Services)
- From mid-2000 to the end of 2010, Michigan is expected to have lost 674,000 jobs, a 14.4 percent decline in total employment. (Source: George Fulton, University of Michigan economist, *The Detroit News*)
- In December 2008, Michigan's unemployment rate hit 10.6 percent, the highest level in 16 years and the worst in the nation. (Source: Michigan Department of Labor and Economic Growth)
- In early December 2008, weekly claims for unemployment insurance benefits hit a 26-year high across the nation, with 573,000 claims filed. (Source: U.S. Department of Labor)
- Michigan workers in four of the top six jobs in Michigan (in terms of having the most workers in a particular job) earn less than the federal poverty level. (Source: U.S. Department of Labor)
- In 2000, Michigan's median household income was \$52,200, whereas the nation's was \$50,000⁷. In contrast, by 2007, the nation's median household income had risen to \$50,700, whereas Michigan's had declined to \$48,000. (Source: U.S. Census Bureau, August 2008)
- From 2001 to 2007, there was a 25 percent jump in Michigan's family poverty rate. (Source: U.S. Census Bureau and 2008 Working Poor Families Report)
- The state of Michigan's food assistance caseload hit a record high of 625,000 households in October 2008. (Source: Michigan Department of Human Services)
- **The number of Michigan citizens without health insurance of any kind has increased to 1.15 million as of 2007.** (Source: U.S. Census Bureau, Health Insurance Coverage Status and Type of Coverage by State)
- The number of Michigan citizens covered by private health insurance plummeted by 727,000 between 1999 and 2007. (Source: U.S. Census Bureau, Health Insurance Coverage Status and Type of Coverage by State)

⁷The dollar amounts from the year 2000 have been inflated to year 2007 dollars for comparability.

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Contact

For more information about this report, contact Peter Schonfeld, senior vice president, Policy and Data Services, at the MHA at (517) 703-8601. Media questions should be directed to Lori Latham, vice president, Political and Public Affairs, at the MHA at (517) 703-8601.

The MHA Policy Staff

Peter Schonfeld, senior vice president, Policy and Data Services
Jason Jorkasky, manager, Finance
Marilyn Litka-Klein, vice president, Health Finance
Vickie Seal, director, Health Finance



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